

Internal Revenue Service

Number: **201604008**

Release Date: 1/22/2016

Index Number: 305.04-00, 305.13-00,
301.00-00, 1385.00-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:CORP:05

PLR-115065-15

Date:

October 22, 2015

Corporation =

State =

Goods and Services =

Stock Exchange =

Predecessor =

Year 1 =

Year 2 =

Year 3 =

Year 4 =

Date =

a =

b =

c =

d =

e =

Dear :

This letter responds to a letter dated April 23, 2015, submitted by your authorized representatives on behalf of Corporation, requesting a ruling regarding the application of sections 301 and 305 of the Internal Revenue Code (the "Code"). The information provided in that letter and in later correspondence is summarized below.

Summary of Facts

Corporation is a cooperative corporation organized as a non-stock, membership association under the laws of State. Corporation is governed by its Board of Directors (the "Board"), which consists of a directors representing b different geographic regions where Corporation does business. The Board is elected by its members, who exercise voting rights based on membership, rather than on equity ownership, and which voting rights conform to the "democratic control" requirements imposed on cooperatives. Corporation is prohibited by the laws of State from paying dividends on its equity at a rate exceeding c% annually.

Corporation provides Goods and Services to its member and nonmember patrons (collectively, "Patrons") and, in accordance with its Articles of Incorporation ("Articles") and Bylaws, conducts this business with Patrons on a cooperative or patronage basis.

Corporation divides its business activities into three segments, and the Board has created allocation units based on these segments (or portions of segments), for purposes of allocating and distributing patronage refunds to Patrons. At the end of each fiscal year, Corporation calculates the net income or loss from patronage business of each of its allocation units. The Board is authorized by the Bylaws to allocate up to d% of the income from patronage business to Corporation's capital reserve. The remaining net income of each allocation unit is then allocated to each Patron in the ratio that the quantity or value of the business done with or for the Patron bears to the quantity or value of the business done with or for all Patrons of such allocation unit.

Corporation annually distributes the income allocated to each Patron as patronage refunds, which qualify as "patronage dividends" (within the meaning of section 1388(a)). The patronage refunds are distributed to Patrons in the year following the fiscal year to which they relate under the rules of subchapter T of the Code. The Bylaws permit the Board to make such distributions in the form of cash, qualified written notices of allocation (within the meaning of section 1388(c)(1)) ("QWNAs"), nonqualified written notices of allocation (within the meaning of section 1388(d)) ("NQWNAs"), revolving fund certificates, securities of Corporation or another entity, or some combination of the

above. Corporation has historically distributed patronage refunds in the form of a combination of cash and QWNAs, and, more recently, NQWNAs.

Each Patron has consented to take into income at its stated dollar amount the portion of any patronage refund made in the form of QWNAs. Corporation deducts from its net income the amount of all patronage refunds distributed in the form of cash and QWNAs in the taxable year to which they relate. Corporation does not immediately deduct at the time of payment, and Patrons do not immediately take into income upon receipt, any patronage refunds paid in the form of NQWNAs. Rather, Corporation and Patrons take NQWNAs into account when redeemed by Corporation.

In addition to its patronage business activity, Corporation also does business with persons who are not Patrons. Corporation separately calculates the revenue and expenses relating to its non-patronage business, and pays federal corporate income tax on the net non-patronage income. Under the Bylaws, such non-patronage income is required to be added to Corporation's capital reserve unless the Board, in its discretion, decides to allocate such income to the allocation units and the Patrons.

Corporation does not issue shares of common stock. Instead, all issued equity interests in Corporation are limited and have a face amount which is payable upon redemption or liquidation of Corporation. That is, all of the holders of Corporation's issued equity have a claim on Corporation's assets that is limited to the equity's face amount. The issued equities of Corporation consist of: capital equity certificates (issued as QWNAs and NQWNAs); non-patronage earnings certificates (together with the capital equity certificates, "Patrons' Equities"); allocated capital reserve; and preferred stock (the "Preferred Stock"). In addition to Corporation's formal, issued equity interests, each Patron of Corporation possesses an unallocated and unissued equity interest (the "Unallocated Equity") in the net assets of Corporation to the extent the value of Corporation's net assets exceeds the face amount of the issued equity interests.

Corporation's capital equity certificates are issued solely to Patrons based on patronage, and are issued on an annual basis as the non-cash portion of patronage refunds. These certificates have a stated dollar face amount, have no maturity date, do not bear interest or dividends, do not entitle the holder any voting rights, cannot be transferred without consent of the Board, and are not subject to redemption upon request of a member. They are redeemed at their face amount on a periodic basis at the discretion of the Board and in accordance with the terms of the redemption policy approved by the Board, which may be modified at any time.

Corporation's non-patronage earnings certificates, issued by a predecessor to Corporation ("Predecessor"), represent an allocation of non-patronage income to members, apportioned on a patronage basis. These certificates have a stated dollar face amount, have no maturity date, do not bear interest or dividends, do not entitle the holder any voting rights, and are not subject to redemption upon request of a member.

They are redeemed at their face amount on a periodic basis at the discretion of the Board and in accordance with the terms of the redemption policy approved by the Board. Patrons take these certificates into account as income under section 61 when redeemed by Corporation. Corporation no longer issues these certificates.

Corporation's allocated capital reserve refers to annual allocations, apportioned on a patronage basis, made by Predecessor to members between Year 1 and Year 2 from amounts that it added to its capital reserve. These allocations were similar to those represented by Corporation's (previously, Predecessor's) non-patronage earnings certificates. Corporation does not redeem allocated capital reserve.

Corporation has also issued various classes of Preferred Stock, both to the general public and to Patrons. Each share of Preferred Stock has an annual dividend at a rate no higher than c%, has a face amount of \$e, and is publicly traded on Stock Exchange. Corporation has not redeemed any shares of Preferred Stock and has no intention to do so.

Corporation's Articles and Bylaws provide that if Corporation is liquidated or dissolved, the net assets of Corporation are to be distributed first to pay the face amount of all Corporation's formal, issued equities. The face amount of the Preferred Stock is required to be distributed to its holders prior to distributions to holders of the face amount of any other equity interest in Corporation. Corporation's remaining assets (the Unallocated Equity) is then to be allocated among the allocation units as the Board determines to be reasonable and equitable considering the origin of such amounts, and the amounts so allocated shall be paid to current and former Patrons of each allocation unit in proportion to their patronage of the unit over such period as may be determined to be equitable and practicable by the Board.

Under Corporation's Annual Redemption Policy, enacted in Year 3, the Board determines the total dollar amount of Patrons' Equities, based on the face amount, eligible for redemption in any year and the portions of this amount that will be redeemed from individuals and from non-individuals. Cash allocated to the redemption of individual Patrons' Equities is applied first to Patrons' Equities held by estates of deceased members and then to Patrons' Equities held by Patrons who have reached the minimum age of redemption for individuals. Cash allocated to the redemption of non-individual Patrons' Equities is limited to the redemption of QWNAs and is applied to such QWNAs in the manner determined by the Board, which has generally applied a first-in, first-out policy but has also limited redemption to those QWNAs held by non-individuals who have done business with Corporation in the preceding five years. In addition, the Board may resolve to redeem additional amounts of individual Patrons' Equities in whatever manner it chooses in its discretion. The Board is authorized to redeem Patrons' Equities not only with cash, but also with other property, including Preferred Stock.

In Year 4, Corporation engaged in an exchange of newly issued shares of its Preferred Stock for outstanding QWNAs. For a number of business reasons, Corporation intends to engage in another exchange (the “Exchange”) of newly issued shares of its Preferred Stock for Patrons’ outstanding QWNAs, on a first-in, first-out basis. Participation by Patrons in the Exchange will be mandatory, but limited to Patrons who hold a minimum amount of QWNAs and have conducted a minimum amount of business with Corporation over a designated, recent timeframe, and may also be limited to non-individual Patrons if, in the judgment of the Board, such limitation is necessary to reduce administrative costs and complexity. The Exchange is expected to take place before Date. The Preferred Stock to be issued in the Exchange will be cumulative preferred stock, with a limited redemption and liquidation value, and will be traded on Stock Exchange. Each share of Preferred Stock issued in the Exchange will be exchanged for QWNAs with a face amount equal to the closing value of a share of Preferred Stock as of a day within 10 days prior to the actual exchange. The total amount of QWNAs to be exchanged and the precise dividend rate on the Preferred Stock will depend upon market conditions.

Representations

Corporation makes the following representations:

1. The Exchange will constitute a recapitalization which qualifies as a tax-free reorganization under section 368(a)(1)(E).
2. None of the Preferred Stock issued in the Exchange will be “nonqualified preferred stock” within the meaning of section 351(g)(2).
3. None of the QWNAs redeemed in the Exchange and none of the Preferred Stock issued in the Exchange will be “section 306 stock” within the meaning of section 306(c).
4. Corporation’s capital equity certificates, non-patronage earnings certificates, allocated capital reserve, Preferred Stock, and Unallocated Equity constitute equity interests in Corporation for federal income tax purposes.
5. At all times, including following the Exchange, the Corporation intends to continue the operation of its business and to continue to operate on a cooperative basis within the meaning of Subchapter T of the Code.
6. The Exchange is not part of a plan to periodically increase the proportionate interest of any equity holder in the assets or earnings and profits of Corporation.

Ruling

Based solely on the information submitted and representations made, we rule that the Exchange will not cause any equity holder in Corporation to be treated as receiving a distribution to which section 301 applies pursuant to section 305(c).

Caveats

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, we express no opinion as to whether Corporation operates as a cooperative under subchapter T, or whether Corporation has appropriately applied the provisions of subchapter T.

Procedural Statements

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

Frances L. Kelly

Frances L. Kelly
Senior Counsel, Branch 2
Office of Associate Chief Counsel (Corporate)

cc: